

THE SOUTHLAND CORPORATION 1979 ANNUAL REPORT

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1979 REVENUES
(Millions)
\$3,463.6 Stores Group
314.7 Dairies Group
97.7 Special Operations Group
and Corporate
\$3,876.0 Total

1979 OPERATING PROFIT
(Millions)
\$145.8 Stores Group
10.3 Dairies Group
7.6 Special Operations Group
\$163.7 Total



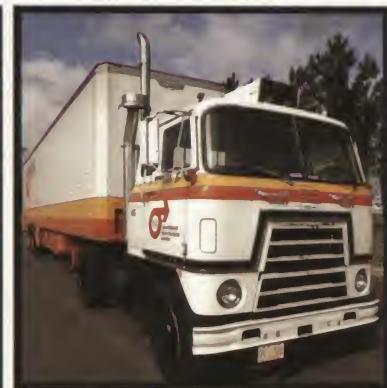
The Southland Corporation, originator of the convenience store concept, is one of the largest retail companies in the United States. Its activities are grouped into three business segments.



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7-ELEVEN The Stores Group is the world's largest operator and franchisor of convenience stores with 6,805 **7-ELEVEN** stores in 42 states, the District of Columbia, and five provinces of Canada. Other retail operations include 105 Gristede's and Charles & Co. food stores and sandwich shops in metropolitan New York, 34 Super Seven multi-pump self-serve gasoline outlets, 467 R S McCall confectionery, tobacco, and news (CTN) stores, and 14 **7-ELEVEN** units in the United Kingdom, as well as an equity interest in 26 Näröppet stores in Sweden and nine Super Siete stores in Mexico. An additional 346 **7-ELEVEN** stores are operated by area licensees in the United States, 774 in Japan, 17 in Australia, and 12 in Canada. The Group also includes four merchandise distribution centers and six sandwich production centers serving **7-ELEVEN** and other customers.



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CORPORATION FILE

 **The Special Operations Group**
includes the Chief Auto Parts,
Chemical, Reddy Ice, and Tidel
Systems Divisions.

 **The Dairies Group** is one of the nation's largest processors of dairy products, which are marketed under 12 well-known regional brand names in 29 states and the District of Columbia.



Jere W. Thompson

John P. Thompson

TO OUR SHAREHOLDERS:

Southland concluded the decade of the '70s with the greatest year in its history.

Stores Group sales were excellent throughout 1979, with 7-Eleven exceeding \$3 billion for the first time, boosting total revenues to \$3.876 billion, up 25.4% over 1978. Convenience store shopping continued to gain in popularity, while consumers responded enthusiastically to prime-time network television advertising and in-store merchandising and promotional programs. The Dairies Group achieved one of its finest years, with record sales and a 53.7% increase in profits, reflecting more favorable market conditions and effective operating and marketing programs. Special Operations Group sales, which for the first time include Chief Auto Parts, more than doubled to \$112.5 million.

At year-end, Southland made three accounting changes. We adopted the last-in, first-out (LIFO) method of determining the cost of

substantially all inventories of the Stores Group. This method more realistically reflects earnings during inflationary periods by matching current costs with current sales and conserves working capital by reducing income taxes. Also, we changed from the deferral to the flow-through method of accounting for investment tax credits (ITC), making the Company's results more comparable with most other retailers and eliminating the future effects of continuing inflation on these credits. While these changes provide immediate and long-term benefits to the Company, financial results for 1979 are not comparable to those of any prior year. In addition, we adopted Statement of Financial Accounting Standards No. 34, which requires the capitalization of interest costs incurred to finance construction or development of properties.

Overall gross margins for the year declined to 24.59% from 25.21% in 1978, primarily reflecting the adop-

tion of LIFO and the effect of the increase in low-margin gasoline sales as a percentage of the total convenience store product mix, from 13.4% in 1978 to 17.2% in 1979. These factors more than offset the improvement in margins for convenience store merchandise, Dairies Group products, and self-serve gasoline. The effect of inflation on inventory costs and rapidly rising gasoline retail prices, without a corresponding increase in gross profit per gallon, will continue to exert pressure on margins.

Net earnings before the accounting changes were a record \$68.3 million, up 19.6% from 1978's \$57.1 million. The cumulative effect of the accounting changes, however, increased earnings to \$83.1 million, up 45.5%. Primary earnings per share were \$3.84, including 72¢ resulting from the accounting changes, compared with \$2.75 in 1978. Diluted earnings were \$3.72, including an additional 70¢, compared with 1978's \$2.66. Per share earnings also reflect the dilutive effect of the two million additional shares of stock issued in August.

Capital expenditures for property, plant, and equipment were \$223 million, the largest single-year investment program in the Company's history. Included was a record \$180.9 million for an accelerated remodeling program and expansion of the Stores Group, which represents 89% of corporate revenues and operating profits. Outlays of \$11.1 million, or 5%, were primarily for the acquisition of Knowlton's dairy and for manufacturing and productivity improvements in the Dairies Group. An additional \$20.3 million, or 9%, was invested in the Special Operations Group for additional capacity, new vehicles, and the expansion of Chief Auto Parts. In late February, 1980, we sold for cash the maintenance facilities, vehicles, and customer leases related to the outside business of Hudgins Truck Rental. The transaction had no material effect on sales or earnings.

FINANCIAL HIGHLIGHTS

(Dollars in thousands except per share data)

	Year Ended December 31		
For the Year	1979	1978	% Change
Total Revenues	\$3,876,059	\$3,090,094	25.4
Net Earnings	83,141	57,097	45.6
Primary Earnings Per Share*	3.84	2.75	39.6
Diluted Earnings Per Share	3.72	2.66	39.8
Cash Dividends	17,382	13,627	27.6
Return on Beginning Shareholders' Equity	22.2%	17.3%	
At Year-End			
Working Capital	168,586	139,633	20.7
Current Ratio	1.55	1.53	
Long-Term Debt	326,893	261,460	25.0
Shareholders' Equity	497,605	374,467	32.9
Book Value Per Share*	23.01	18.01	27.8
Annual Dividend Rate Per Share	.84	.72	16.7
Average Shares Outstanding (000's)	21,626	20,787	4.0
Number of Shareholders	8,708	8,627	0.9
Number of Employees	44,300	37,000	19.7

*Based on average number of shares outstanding during the period after adjusting for all stock dividends.

EFFECT OF ACCOUNTING CHANGES ON 1979 EARNINGS

(Dollars in thousands except per share data)

	Earnings Per Share		
	Amount	Primary	Diluted
Net Earnings before any changes	\$68,273	\$3.16	\$3.06
Accounting Changes:			
LIFO	(8,613)	(.40)	(.38)
Capitalization of interest	2,010	.09	.09
Current year ITC	6,603	.31	.29
Cumulative ITC	15,665	.72	.70
Contribution to Profit			
Sharing on cumulative ITC	(797)	(.04)	(.04)
Net Earnings after all changes	83,141	3.84	3.72
Remove effect of cumulative ITC	(15,665)	(.72)	(.70)
Net Earnings before cumulative ITC	67,476	3.12	3.02
Remove effect of contribution to Profit			
Sharing on cumulative ITC	797	.04	.04
Pro Forma Net Earnings	\$68,273	\$3.16	\$3.06

To provide the additional capital necessary to support our growth, the Company in August sold two million shares of common stock and \$75 million of unsecured 9½% Sinking Fund Debentures. The new debt, as well as the Company's two prior debenture issues, is rated "A" by both Moody's and Standard & Poor's.

Cash dividends paid during the year were \$17.4 million, up 27.5%

from the prior year, and in April the annual rate was raised 16.7% to 84¢ a share. Each year since 1957 cash dividends have been paid, and during the past nine years the rate has been increased eight times, providing shareholders an average annual compound growth of 20%. In addition, for the 14th consecutive year, a 3% stock dividend was distributed.

The Company continues to encourage the "Southland family" to participate in community activities of the thousands of neighborhoods we serve. The most ambitious Company-wide project has been four years as the largest corporate fundraiser for the Muscular Dystrophy Association. Employees, franchisees, shareholders, suppliers, and customers have collected more than \$15.7 million for the Jerry Lewis Labor Day Telethon, including \$4.23 million in 1979. In addition, the Dairies Group is a national corporate sponsor of the March of Dimes, assisting that organization with the Mother's March on Birth Defects.

During the year, major investments were made in personnel training and development programs to reinforce Southland's organizational structure and to ensure that it is responsive to our changing needs. We also strengthened our senior management team with the election of two Executive Vice Presidents and two Vice Presidents, and in April two newly created Directorships on the Board were filled.

Southland set records in both revenues and earnings each year of the past decade in a highly competitive and unpredictable business, political, and social environment. These achievements would not have been possible without the loyalty and dedication of our employees, franchisees, and shareholders. With their continuing support, we look forward to greater accomplishments in the '80s.

JOHN P. THOMPSON
CHAIRMAN

JERE W. THOMPSON
PRESIDENT

1970s

Getting Ready for the '80s

During the past decade, a series of unprecedented events challenged the strength and resourcefulness of Southland and the convenience store industry.

The '70s began with the close of one recession, ended with the threat of another, and between them were disruptive energy shortages, escalating inflation, increasingly restrictive governmental regulations, the Watergate dilemma, environmental activism, far-reaching social and economic changes, remarkable technological advances, and the most severe recession since the '40s.

Yet Southland's operating philosophy and adaptability to change enabled the Company to turn many of these challenges into opportunities for greater growth and success and to become one of the largest retailers in the United States.

Led by 7-Eleven, Southland attained its first billion dollar sales year in 1971, reached two billion in 1976, three in 1978, and achieved its first billion dollar quarter in 1979. In 1974, the 5,000th 7-Eleven store was opened, and in 1977, the Company celebrated its Golden Anniversary — 50 years of providing fast, friendly, convenient shopping in neighborhoods across the country. Also during the '70s, Southland expanded the convenience store concept into a number of domestic and international markets through license agreements, and now makes convenience shopping available at almost 9,000 7-Eleven and other retail outlets throughout the world.

Our Dairies and Special Operations Groups complemented this exceptional growth. The first Distribution and Food



THE 1980s

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CORPORATION



Processing Centers, designed to service the unique requirements of thousands of 7-Eleven stores, were opened in 1971 as part of a program that spanned the decade, with the second and third Centers completed in 1973, and a fourth in 1979. The Dairies Group more than doubled its volume and now is one of the largest fluid milk processors and distributors in the nation.

To sustain the momentum of the '70s, we have developed our human resources into a strong and capable team, reinforced the organizational structure, built a solid financial foundation, and implemented extensive management information and internal control systems, all of which provide support and cohesiveness to our wide-spread and diverse operations.

Looking to the '80s, we intend to maintain Southland's position of leadership in the convenience store industry, further strengthen the Company's financial standing, and apply our retailing knowledge to expand the range of products and services offered to consumers around the world. The "Southland family" will maintain its tradition of community involvement, and at the same time, the Company will continue to be a responsible corporate citizen, fulfilling its obligations to shareholders, employees, franchisees, suppliers, and the public it serves.

We believe in the future of the convenience store industry — the most vigorous sector of food retailing — and in Southland's ability to meet the challenges of the '80s through its time-proven formula for success: "Give the customers what they want, when they want it, where they want it."



Stores Group

(Millions)	1975	1976	1977	1978	1979	5 Year Compound Growth
Sales	\$1,555.0	\$1,854.9	\$2,267.8	\$2,784.0	\$3,453.0	19.7%
Operating Profit	80.8	92.3	115.7	142.7	145.8	16.3

Outstanding Sales Gain

7-ELEVEN ended the decade with its first 3 billion dollar year, reaching \$3.211 billion in sales, up 23.7% over last year's \$2.595 billion. The record-setting pace, evident throughout the year, was due to the continuing popularity of convenience store shopping, enthusiastic consumer response to effective prime-time network television advertising, stepped-up merchandising and promotional programs, and a substantial increase in demand for self-serve gasoline. In addition, more efficient use of selling space and higher volume in established stores, competitive pricing of selected items, the opening of new stores, and the introduction of new products contributed to the outstanding gain.

Sales of the Stores Group increased \$669.0 million to \$3.453 billion, up 24.0%, and represented 90% of Company sales.

Growth Continues

At year-end, there were 6,805 **7-ELEVEN** stores open, including 4,184 Company operated and 2,621 franchised, in 42 states, the District of Columbia, and five provinces of Canada. Although 666 stores were opened, 460 were closed because of relocation of older units to newly available and more desirable sites, population shifts, changing neighborhood and traffic patterns, lease expirations, and unacceptable levels of profitability.

7-ELEVEN Is Convenience

The key to the success of **7-ELEVEN** is giving customers what they want, when they want it, where they want it. To almost six million people a day, convenience means fast in-and-out shopping around the clock, easy access to a broad product selection, and friendly service. Their purchases, averaging \$1.73, provide a continuous stream of market research data which is used to determine how best to satisfy the changing needs and wants of **7-ELEVEN** customers.

Time-conscious customers look to **7-ELEVEN** for a fast on-the-go meal.

More than 80% choose "their" store because it is conveniently located in the neighborhood where they live or work. Hours of operation also are important, with about 96% of all stores open longer than the traditional 7 a.m. to 11 p.m., including 5,847 which never close. Customers average 4.4 trips per week to **7-ELEVEN** stores, with 35% of their visits on weekends.

Almost 70% of customers are male, although the number of women shoppers is increasing as they continue to enter careers outside the home. While customers of all ages shop **7-ELEVEN**, approximately half are in the 25-54 age group. This group is expected to increase to 103 million by 1990, a gain of approximately 18.4 million potential customers.

Gasoline Sales Up

During the '70s, gasoline steadily increased in importance to the **7-ELEVEN** sales mix — from less than 1% to more than 17% — as more and more motorists accepted the self-serve concept. From a base of 59 installations in 1970, Southland, to accommodate the demand for this new and popular service, expanded facilities to 2,107 stores by the end of 1979, 250 more than in 1978.

As a result of supply shortages, which began during the first quarter, total gallonage increased only 10%, but substantial retail price increases due to escalating crude oil costs pushed sales up 61% for the year.



Fashionable sunglasses were one of many popular seasonal promotions.

As approximately 31% of gasoline customers, many new to **7-ELEVEN**, purchase other items, those stores offering this product benefited from additional sales.

Southland also operates 34 multi-pump self-serve units, principally on the West Coast, most of which were acquired in 1976 as part of the purchase of a group of potential **7-ELEVEN** sites from an oil company. Sales of these high-volume "Super Seven" stations are not included in **7-ELEVEN** gasoline revenues.

Network Advertising Increasing

Southland substantially enlarged its nationwide prime-time television advertising following the extremely successful first campaign in 1978. Members of approximately 67 million households each broadcast week were invited to visit their neighborhood **7-ELEVEN** for a breakfast of freshly brewed coffee and delicious Danish pastry, "Egg Hamlette," or "Sausage and Biscuit." The campaign also featured such popular **7-ELEVEN** sandwiches as "Big' Un," "Ham and Cheese," "Submarine," and "Chili Dog," and for an anytime taste treat, the "Big Wheel," an ice cream confection. And, for the first time, Southland advertised milk on network television in May, reminding America that "**7-ELEVEN** is the dairy store." The well received television campaign, supplemented in selected markets by extensive radio and newspaper advertising, increased customer awareness of **7-ELEVEN** fast food items and resulted in significantly higher sales.

Remodeling Accelerates

An accelerated store remodeling program was begun in 1979, and by year-end, more than 1,100 units had been completed with an additional 1,900 scheduled over the next two years. Projects range from changing store layouts to accommodate demand for **7-ELEVEN** fast foods and self-serve gasoline to extensive renovation of the stores' interiors and exteriors, including installation of new, more energy-efficient equipment. Positive customer response to the bright, attractive, remodeled stores has substantially increased sales.



On network TV, hot **7-ELEVEN** coffee soothed the monster in early risers, while the "Drugstore Cowboy" introduced "Big Gulp" in test markets.



Personnel Development Emphasized

During the year, Southland introduced a "Certified Store Managers" program as part of its continuing recognition of the long-term benefits of personnel training and development to both the Company and its employees. Designed to increase the management skills of new and veteran managers, the program includes three days of classroom instruction in merchandising, inventory control, security, administrative procedures, and management principles, followed by an extended period of in-store training and evaluation. Upon successful completion of both phases of the training program, managers are certified and qualify to participate in a new compensation plan which recognizes their higher level of professionalism. In 1979, 3,545 store managers completed the classroom training, and almost 500 have met the additional performance requirements for certification.

New York City Convenience

The 105 Gristede's stores serve the greater New York area with select meats, fresh produce, and a full line of premium-quality groceries. A number of stores offer "big city" convenience through such specialized services as telephone ordering, home delivery, and charge accounts. The Division's Charles & Co. shops feature made-to-order sandwiches, delicatessen items, snacks, and beverages, while the gourmet stores offer a tempting variety of specialty foods and gift-packaged delicacies.



"Slurpee,"
Danish pastries,
and a wide
selection of
sandwiches are
7-ELEVEN favorites.



completed in October for the development of **7-ELEVEN** stores in Taiwan.

Sales of international operations and area licensees are not included in Southland's revenues, but earnings of affiliates and royalties from licensees based upon sales are reported as Other Income.

Food Centers Added

The trends that established convenience stores as the fastest-growing segment of food retailing are also contributing to the demand for "food away from home." Higher family incomes, changing lifestyles, greater numbers of career women, smaller families, more single people, and the growing mobility of the population have changed "eating out" from a special occasion to a common occurrence.

Southland's fast foods program continues to capture a greater share of this growing market with a popular line of about 30 sandwiches packaged under the **7-ELEVEN** and Landshire labels. The sandwiches, either fresh or flash-frozen for convenient heating in microwave or infrared ovens, are distributed to **7-ELEVEN** stores, other retailers, and institutional customers. The Centers also produced more than one million gallons of syrup for "Slurpee," the refreshing **7-ELEVEN** semi-frozen carbonated drink.

A fifth Food Center was opened in early October at the new Distribution Center in Illinois, while the sixth was completed at Salt Lake City in early December. In response to the increasing popularity of Mexican-style fast foods, the newest and largest Center will also produce burritos for distribution nationwide. The burrito production line is the most modern in the United States, with an annual capacity in excess of 40 million units.

An experienced staff of architects and engineers coordinates store construction.



Distribution System Extended

Four regional Distribution Centers provide a unique, highly sophisticated merchandise distribution system which assures **7-ELEVEN** stores a reliable and efficient source of supply and frequent deliveries scheduled to maintain high in-stock position.

The system enables the stores to order pre-priced merchandise in less than case lots, improve inventory turnover, stock fresher merchandise, and use selling space more profitably. In addition, it provides the stores greater flexibility to change their product assortment in response to customer preferences and seasonal demands, undertake promotional programs, and introduce new products.

Located in Virginia, Texas, Florida, and Illinois, the Centers were serving 4,437, or 65%, of all **7-ELEVEN** stores at year-end and contributed significantly to profits. Sales for the year were up 28.6% to \$488.2 million, including \$29.2 million to outside customers.



The new "Certified Store Manager" program improves management skills.



Percent Convenience Stores Sales (by Principal Product Category)

	1979	1978	1977	1976	1975
Gasoline	17.2%	13.4%	9.8%	6.8%	3.9%
Tobacco Products	12.9	12.9	14.2	14.7	15.6
Groceries	12.6	13.4	14.0	14.6	15.3
Beer/Wine	12.4	12.9	13.7	14.4	14.8
Soft Drinks	10.3	10.9	11.0	10.7	11.5
Non-Foods	8.7	9.4	9.9	10.2	9.5
Dairy Products	8.4	8.9	9.3	9.6	9.9
Other Food Items	6.2	5.5	4.7	4.7	4.2
Candy	4.3	4.7	5.0	5.4	5.7
Baked Goods	3.8	4.6	5.0	5.3	5.7
Health/Beauty Aids	3.2	3.4	3.4	3.6	3.9
Total	100.0%	100.0%	100.0%	100.0%	100.0%

The Company does not record sales by product lines but estimates the percentage of convenience store sales by principal product category based upon total store purchases.

The distribution process begins with the completion at the store of a computer-generated order list customized to meet each store's merchandise requirements. These orders are transmitted by each **7-ELEVEN** district office through its computer terminal to the Company's computer center in Dallas, where the information is assimilated and transmitted to printing terminals at the appropriate Distribution Center. The orders are then "picked" and assembled for delivery on specially designed trucks with separate compartments for dry, chilled, and frozen merchandise. The entire cycle of merchandise movement — replenishing the Centers' inventories, truck loading sequence, and the most time and energy efficient routing of vehicles — is scheduled by computer. The Centers achieved an average annual inventory turnover of 19 times and, for the sixth consecutive year, a 99% order fill rate.

Southland's newest Center in Champaign, Illinois, began deliveries in October and will serve **7-ELEVEN** stores in 11 midwestern states. The facility was serving 552 stores at year-end and is scheduled to phase in about 500 more in 1980.

Recognizing that others can benefit from many of the same services enjoyed by **7-ELEVEN**, the Centers are actively developing outside business with fast food outlets, restaurants, hotels, airline caterers, drug store chains, and others. To service these new customers, more than 200,000 square feet of additional dry, refrigerated, and freezer space were completed at the three other Centers.



SDC deliveries
are computer-
scheduled for
time and energy
savings.





Dairies Group

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(Millions)	1975	1976	1977	1978	1979	5 Year Compound Growth
Outside Sales	\$208.1	\$235.7	\$235.9	\$252.8	\$313.9	11.3%
Intracompany Sales	89.6	103.6	125.8	135.6	158.6	13.0
Total	297.7	339.3	361.7	388.4	472.5	11.9
Operating Profit	10.1	8.6	6.0	6.7	10.3	5.1

Outstanding Year

The Dairies Group, with 28 processing plants and 83 distribution branches, closed out the '70s with one of the finest years in its history. Total sales increased 21.7% to \$472.5 million, while operating profits rose 53.7% to \$10.3 million. Sales to outside customers were \$313.9 million, up 24.2%, and represented 8% of total corporate sales. Intracompany sales increased 17.0% to \$158.6 million. The Dairies serve 5,303 **7-ELEVEN** stores, supplying them with 62% of all dairy products sold.

Operating profits increased substantially from the 1978 level. Favorable market conditions and aggressive merchandising enabled the Dairies Group to improve margins, even though farm milk costs, distribution, and other business expenses continued to rise. The Group also benefited from effective expense controls and the efficiencies realized from its on-going plant modernization and automation programs.

Expansion Continues

Remodeling and expansion projects in 1979 included additional capacity at Cabell's in Dallas and Velda Farms in Miami. Recently, construction began on a new Velda Farms distribution branch to serve the rapidly growing Orlando, Florida, market. In April, Knowlton's Inc., a family-owned San Antonio dairy, was purchased by Southland, enabling the Dairies Group, in the most cost effective manner, to expand its fluid milk processing and distribution capabilities into the south Texas market.

During the year, greater emphasis was placed on marketing higher margin products, particularly the increasingly popular line of frozen dairy novelties. Nationwide prime-time television advertising included commercials on the "Big Wheel" and, for the first time, milk. The "Big Wheel" and "Big Deal," coated ice cream confections, continued to be customer favorites along with the new "Naturally Yours" line of all-natural, sundae-style yogurts, which was introduced in the fall.



The Dairies Group distributes fine dairy products under 12 well known regional names: Adohr Farms, Bancroft, Briggs, Cabell's, Embassy, Harbinsons, Horten's, Knowlton's, Midwest Farms, Oak Farms, Velda Farms, and Wanzer's.



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Special Operations Group

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(Millions)	1975	1976	1977	1978	1979	5 Year Compound Growth
Outside Sales	\$24.8	\$25.2	\$32.4	\$39.7	\$ 89.3	32.4%
Intracompany Sales	13.6	13.3	14.5	15.3	23.2	11.2
Total	38.4	38.5	46.9	55.0	112.5	25.9
Operating Profit	0.9	6.4	6.7	6.0	7.6	13.5

Sales and Profits Increase

The Special Operations Group consists of diversified operations which distribute products and provide services to a growing number of outside customers, as well as to Southland. Group sales, which for the first time include Chief Auto Parts, more than doubled to \$112.5 million, while operating profits rose 24.6% to \$7.6 million. Outside sales were \$89.3 million, representing 2% of total corporate sales, while intracompany sales were \$23.2 million, 51.6% greater than last year.

Chief's First Year

Southland acquired Chief Auto Parts, a chain of 119 retail automobile supply stores in southern California, at the end of 1978.

Chief's products are popular with do-it-yourselfers. Other divisions supply ice, cash controllers, and specialty chemicals for many industries.

The stores, typically 2,000 square feet in size, offer approximately 6,500 replacement parts and accessories and feature nationally known brands, as well as some private-label items.

With more than half of all car owners now performing at least part of their own maintenance, the do-it-yourself auto parts market has tremendous growth potential and provides Southland an opportunity to adapt its convenience store expertise to another field of retailing.



In April, Chief entered the Dallas-Fort Worth area with the acquisition of 19 stores. Two Las Vegas stores were opened in September, and the Division is studying other markets in the Sunbelt as part of its growth plans. At the end of the year, 171 stores were operating, including 131 in southern California, 36 in Texas, and 4 in Nevada, with another 12 scheduled to open in the near future.

Chemical Broadens Line

The Chemical Division produces a broad line of specialty chemical products for domestic and international customers in the food processing, textile, leather tanning, oil field services, pharmaceutical, agricultural, and dairy processing industries. Sales increased 19.3% for the year, with outside customers representing 80% of total volume.

With manufacturing plants in Illinois, Texas, New Jersey, and Florida, the Division's product line includes coatings, can sealants, emulsifiers, dough strengtheners and softeners, leather tanning compounds, surfactants used in such products as synthetic detergents and soaps, and agricultural, pharmaceutical and other industrial intermediates. Many of its products are also supplied to Southland operations, such as "Slurpee" concentrates, food ingredients, flavorings, preservatives, sanitizers, and cleansing agents.

During the year, the Great Meadows, New Jersey, plant began manufacturing and marketing a line of chemicals used by pharmaceutical companies in producing antihistamine compounds. This facility is being expanded to process a group of neutralizing agents used in the production of resins. In addition, both the Dallas and Chicago facilities increased their production capacity for sodium acetate, a compound used as a preservative or to control relative acidity or alkalinity in many industrial processes.

Reddy Ice Adds Capacity

Reddy Ice, with plants in Dallas, Waco, Houston, Austin, Ft. Lauderdale, and Las Vegas, manufactures and distributes packaged and commercial ice through **7-ELEVEN** stores and other outlets. The Division serves markets in Arizona, Arkansas, California, Florida, Louisiana, Nevada, Texas, and Utah.

Annual production capacity was increased to almost half-a-million tons with the addition of equipment at four existing plants, as well as the opening in early summer of a new Dallas plant, the largest fully-automated ice manufacturing facility in the United States. Sales volume, 68% of which was to outside customers, was only slightly higher, however, as unusually cool summer weather reduced demand from the record 1978 level.

Following successful test-marketing in 1978, the Division expanded distribution of "Reddy Wood" to **7-ELEVEN** and other retailers in Texas. The addition of the small carry-out bundles of high-quality firewood to its product line will enable Reddy Ice to increase sales and profits, as well as better balance highly seasonal labor and equipment requirements.

Tidel Increases Production

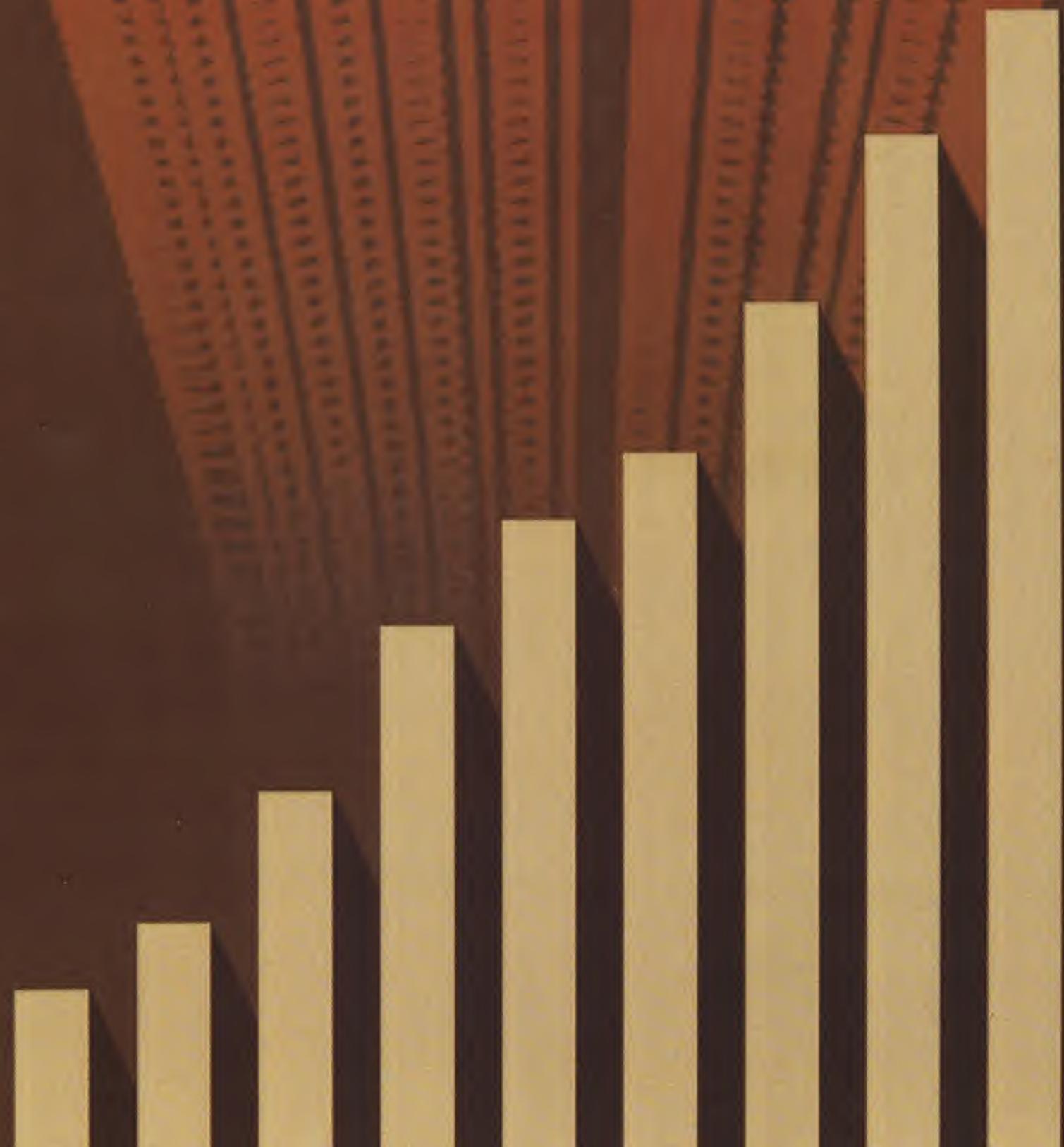
Tidel Systems stepped up production of its innovative "Timed Access Cash Controller" (TACC) money holding device designed specifically for use by **7-ELEVEN** and other cash-oriented retailers. The minicomputer controlled TACC provides cash handling efficiency and security, as well as customer convenience, by permitting the withdrawal of specific amounts of cash at preset time intervals, while all other money remains secured in a hardened "safe" area.

Up to now, virtually all of Tidel's production has been required to supply TACCs to **7-ELEVEN**. However, this program will be completed in 1980, and Tidel's marketing efforts are now being directed toward other retailers, who have expressed great interest in the cash controller. Branch offices have been opened in Dallas, Houston, Atlanta, Chicago, and Los Angeles as part of Tidel's program to establish a nationwide sales and service organization.



Tidel manufactures its innovative TACC at a new Dallas plant.

Financial Review



FINANCIAL SUMMARY**THE SOUTHLAND CORPORATION AND SUBSIDIARIES**

(Dollars in thousands except per share data)

	1979	1978	1977	1976	Years Ended December 31
					1975
Operations (Note 1)					
Total revenues	\$3,876,059	\$3,090,094	\$2,545,415	\$2,122,023	\$1,790,805
Increase over prior year	25.43%	21.40%	19.95%	18.50%	10.94%
Net earnings	83,141	57,097	45,317	37,849	32,068
Increase over prior year	45.61%	25.99%	19.73%	18.03%	18.04%
Per revenue dollar	2.14%	1.85%	1.78%	1.78%	1.79%
Return on beginning shareholders' equity	22.20%	17.30%	15.62%	14.56%	13.72%
Pro forma net earnings (Note 2)	68,273	60,357	47,664	40,037	33,717
Increase over prior year	13.12%	26.63%	19.05%	18.74%	19.93%
Assets Employed (Note 1)					
Working capital	168,586	139,633	136,693	101,536	80,196
Current ratio	1.55	1.53	1.66	1.63	1.58
Property, plant, and equipment including capital leases (net)	838,796	677,284	567,442	506,190	447,392
Depreciation and amortization	79,111	67,724	61,735	55,029	47,974
Total assets	1,367,575	1,134,476	942,531	799,261	696,107
Capitalization (Note 1)					
Long-term debt	326,893	261,460	195,520	153,093	119,911
Capital lease obligations	226,257	211,342	192,547	178,556	163,380
Shareholders' equity	497,605	374,467	329,952	290,142	259,940
Total capitalization	1,050,755	847,269	718,019	621,791	543,231
Shareholders' equity to total capitalization	47.36%	44.20%	45.95%	46.66%	47.85%
Per Share Data (Notes 1 and 3)					
Primary earnings	3.84	2.75	2.20	1.86	1.58
Earnings assuming full dilution	3.72	2.66	2.13	1.80	1.53
Pro forma primary earnings (Note 2)	3.16	2.90	2.31	1.97	1.67
Pro forma earnings assuming full dilution (Note 2)	3.06	2.81	2.24	1.90	1.61
Cash dividends80	.66	.53	.43	.35
Shareholders' equity	23.01	18.01	16.00	14.25	12.85
Other Data					
Cash dividends	17,382	13,627	10,961	8,660	7,033
Dividends as a % of net earnings (Note 1)	20.91%	23.87%	24.19%	22.88%	21.93%
Stock dividends	3%	3%	3%	3%	3%
Average shares outstanding (Note 4)	21,626,397	20,787,335	20,615,977	20,354,641	20,232,235
Average diluted shares (Note 4)	22,591,135	21,763,673	21,658,987	21,538,378	21,510,230
Market price range (Note 4)					
High	31½	32¾	25½	25¾	25½
Low	24¾	20⅓	18¾	18½	13½
Year-end	28¾	26	23¾	24¾	19¾
Number of shareholders	8,708	8,627	8,764	8,881	9,093
Number of employees	44,300	37,000	34,000	31,000	28,600

Notes:

- (1) The years 1975 through 1977 have been restated for the change in the method of accounting for leases to comply with the provisions of Statement of Financial Accounting Standards No. 13.
- (2) Earnings data for the years 1975 through 1978 have been restated to reflect the change in accounting for investment tax credits.
- (3) Based on average shares outstanding adjusted for stock dividends.
- (4) Adjusted for stock dividends.

1979 Accounting Changes

(1) The Company adopted the last-in, first-out (LIFO) method of determining the cost of substantially all inventories of the Stores Group. This method more realistically reflects earnings during inflationary periods by matching current costs with current sales and conserves cash by reducing income taxes.

(2) The Company changed from the deferral to the flow-through method of accounting for investment tax credits (ITC). This change makes the

Company's results more comparable with most other retailers, eliminates the future effects of continuing inflation on these credits, and reflects the current impact of capital investment decisions on earnings.

(3) The Company adopted Statement of Financial Accounting Standards No. 34, which requires the capitalization of interest costs incurred to finance construction or development of properties.

The current year's financial statements are not comparable to

those of any prior year, as restatement is not permitted for any of the above accounting changes. However, pro forma earnings, which may be shown, remove the cumulative effect of the accounting change for ITC and present prior years as if on the flow-through method. Therefore, Southland believes that the most meaningful comparison is on the pro forma basis.

The effect of the accounting changes on net earnings is as follows (000's omitted):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Net earnings before any changes	\$ 8,131	\$22,435	\$24,017	\$13,690	\$68,273
Accounting changes:					
LIFO	(2,234)	(1,698)	(2,454)	(2,227)	(8,613)
Capitalization of interest	557	385	492	576	2,010
Current year ITC	314	2,372	2,480	1,437	6,603
Cumulative ITC	15,665	—	—	—	15,665
Contribution to Profit					
Sharing on cumulative ITC	(797)	—	—	—	(797)
Net earnings after all changes	21,636	23,494	24,535	13,476	83,141
Remove effect of cumulative ITC	(15,665)	—	—	—	(15,665)
Net earnings before cumulative ITC	5,971	23,494	24,535	13,476	67,476
Remove effect of contribution to Profit Sharing on cumulative ITC	797	—	—	—	797
Pro forma net earnings	\$ 6,768	\$23,494	\$24,535	\$13,476	\$68,273
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Primary earnings per share:					
After all changes	1.04	1.13	1.12	.55	3.84
Before cumulative ITC	.29	1.12	1.14	.57	3.12
Pro forma	.33	1.12	1.14	.57	3.16
Diluted earnings per share:					
After all changes	1.00	1.09	1.08	.55	3.72
Before cumulative ITC	.28	1.09	1.09	.56	3.02
Pro forma	.32	1.09	1.09	.56	3.06



A wide range of private-label products are available at 7-ELEVEN.

Revenues

Revenues reached an all-time high of \$3.876 billion, up \$786.0 million over the record \$3.090 billion in 1978. For the first time in the Company's history, revenues for a quarter topped one billion dollars, with both the third and fourth periods exceeding that amount. Continued acceptance of convenience store shopping, the net addition of 206 7-Eleven stores, more favorable dairy market conditions, and a substantial increase in demand for self-serve gasoline contributed to the exceptionally strong 25.4% gain, although an unprecedented level of inflation also influenced results. The Stores Group represented 89% of total corporate revenues, while the Dairies Group accounted for 8%, and the Special Operations Group the remaining 3%.

7-Eleven volume, 83% of Company sales, rose \$616.6 million to \$3.211 billion, a gain of 23.8%. An increase in merchandise sales of \$402.2 million, representing 15.5% of the gain, resulted from more efficient use of selling space and higher volume in established stores, successful prime-time network television advertising,

and stepped-up promotional and in-store merchandising programs, as well as additional 7-Eleven units. An increase in gallonage, together with frequent price adjustments during the year, resulted in self-serve gasoline volume being up \$214.4 million, or the remaining 8.3% of the total gain. Sales of the Stores Group were up 24.0%, while the Dairies Group increased 24.2%, and the Special Operations Group, including Chief Auto Parts for the first time, showed a gain of 124.9%.

Revenues (Millions)

QUARTER	1979	1978	% Gain
First	\$ 812.1	\$ 648.8	25.2
Second	959.6	777.6	23.4
Third	1,059.6	848.3	24.9
Fourth	1,044.7	815.4	28.1
TOTAL	\$3,876.0	\$3,090.1	25.4

Net Earnings

Net earnings before the cumulative effect of the accounting change for ITC were a record \$67.4 million, up \$10.3 million or 18.0% from 1978 earnings of \$57.1 million. The

excellent gain over the prior year was primarily the result of a strong 25.3% increase in sales, stable dairy market conditions, and improved gross margin on both convenience store merchandise and self-serve gasoline.

Pro Forma Net Earnings (Thousands)

QUARTER	1979	1978	Gain
First	\$ 6,768	\$ 7,461	(9.3)
Second	23,494	19,071	23.2
Third	24,535	19,992	22.7
Fourth	13,476	13,833	(2.6)
TOTAL	\$68,273	\$60,357	13.1

The cumulative effect of the accounting change for ITC increased earnings an additional \$15.7 million to a total of \$83.1 million, up 45.5%. Pro forma earnings, which remove the cumulative effect of the accounting change for ITC from the current year earnings and present prior years as if the flow-through method had been in effect, were \$68.3 million for 1979, up 13.1% from 1978 earnings of \$60.4 million.

REVENUES (Millions)**Compound Growth Rate: 19.1%**

Stores Group	\$1,556.0	\$1,857.5	\$2,271.9	\$2,791.0	\$3,463.6
Dairies Group	208.3	236.1	236.5	253.4	314.7
Special Operations Group	25.0	26.0	33.7	40.9	90.7
Corporate	1.5	2.4	3.3	4.8	7.0
TOTAL	\$1,790.8	\$2,122.0	\$2,545.4	\$3,090.1	\$3,876.0

**NET EARNINGS (Millions)****Compound Growth Rate: 25.1%**

Earnings increased \$15.7 million for cumulative effect of changing to flow-through method of accounting for ITC.

\$32.1	\$37.8	\$45.3	\$57.1	\$83.1
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Earnings Per Share

Primary earnings per share were \$3.84, including 72¢ resulting from the accounting changes, compared with \$2.75 in 1978. Pro forma earnings were \$3.16, up 9.0% over 1978 earnings of \$2.90. Average shares outstanding were 21,626,397, up 4.0% compared with the prior year's 20,787,335.

Pro Forma Primary*

QUARTER	1979	1978	% Gain
First	\$.33	\$.36	(8.3)
Second	1.12	.92	21.7
Third	1.14	.96	18.8
Fourth	.57	.66	(13.6)
TOTAL	\$3.16	\$2.90	9.0

Assuming full dilution, earnings per share were \$3.72, including 70¢ from the changes, compared with \$2.66 in 1978. Pro forma earnings were \$3.06, up 8.9% from 1978 earnings of \$2.81. Diluted earnings were computed on the basis of 22,591,135 average shares, up 3.8% compared with 21,763,673 a year earlier.

Pro Forma Diluted*

QUARTER	1979	1978	% Gain
First	\$.32	\$.35	(8.6)
Second	1.09	.89	22.5
Third	1.09	.93	17.2
Fourth	.56	.64	(12.5)
TOTAL	\$3.06	\$2.81	8.9

*Adjusted for 3% stock dividend in each year.

Dividends Paid Per Common Share

CASH:	QUARTER	1979	1978
First	\$.18	\$.15	
Second	.21	.18	
Third	.21	.18	
Fourth	.21	.18	
TOTAL	\$.81	\$.69	
STOCK:		3%	3%

In April, 1979, the annual rate was increased 16.7% to 84¢ a share from 72¢. Southland has raised its cash dividend rate eight times in the past nine years, providing shareholders a compound growth rate of 20%. Total cash dividends distributed during the year were \$17,381,682, an increase of 27.5% over the \$13,627,443 paid the previous year, representing 20.9% of net earnings. Although no fixed dividend payout percentage has been established, future payments are expected to range between 20-30% of annual earnings as they have for the past six years.

PRIMARY EARNINGS PER SHARE

(Dollars)

Compound Growth Rate: 22.7 %

■ Per share earnings increased 72¢ for cumulative effect of changing to flow-through method of accounting for ITC.

\$1.58 \$1.86 \$2.20 \$2.75 \$3.84



DIVIDENDS (Millions)

Compound Growth Rate: 24.4 %

\$7.0 \$8.7 \$11.0 \$13.6 \$17.4



SHAREHOLDERS'

EQUITY PER SHARE (Dollars)

Compound Growth Rate: 14.2 %

\$12.85 \$14.25 \$16.00 \$18.01 \$23.01



Shareholders' Equity

Shareholders' equity rose to \$497.6 million at year-end, compared with \$374.5 million the prior year. The \$123.1 million increase resulted from retained earnings of \$46.4 million and \$76.7 million additional paid-in capital.

At December 31, 1979, 22,935,504 shares of common stock were outstanding, compared with 20,200,557 shares a year earlier, an increase of 2,734,947 shares. The 13.5% increase resulted primarily from the public sale of two million shares in August, 1979. Also, 664,198 shares were issued in payment of a 3% stock dividend, 21,384 upon conversion of 5 1/4% Convertible Subordinated Notes, 17,978 in an acquisition, 30,341 shares under the key employees incentive plan, and 1,046 upon exercise of stock options. At year-end, 877,800 shares were reserved for issuance upon conversion of outstanding debentures and 569,622 for issuance under the stock option and key employees incentive plans.

Return on equity, an important investment ratio, reflects both the return on total invested capital and the degree of leverage employed. Southland's return on beginning shareholders' equity (net earnings divided by equity) increased in 1979 to

22.2%, substantially above the 14.9% average of the past five years.

Book value per share (shareholders' equity divided by average shares outstanding) was \$23.01, compared with \$18.01 at the close of 1978, an increase of 27.8%.

Financial Position

Working capital (current assets minus current liabilities) increased \$29.0 million to \$168.6 million at the close of 1979, compared with \$139.6 million the previous year. The ratio of current assets to current liabilities (assets divided by liabilities) was 1.55 to 1, compared with 1.53 to 1 a year earlier.

Southland has traditionally utilized the most advantageous combination of funds from operations, debt, equity, and lease financing to provide the capital necessary for planned sales and earnings growth through expansion and remodeling of existing facilities, acquisitions, and new ventures. In keeping with this program, two million shares of common stock were sold in August, 1979, and a simultaneous long-term financing of \$75 million 9 1/2% Sinking Fund Debentures due August 15, 2004, was completed. The new debt, as well as the Company's 8 3/8% and 9 3/8% debenture issues, is rated "A" by both Moody's

and Standard & Poor's. In addition, early in 1979 the Company, for the first time, issued a limited amount of commercial paper, which was rated A-2 by Standard & Poor's and P-2 by Moody's, to establish an alternate method of financing short-term working capital requirements at more attractive interest rates. As of December 31, 1979, long-term debt was \$326.9 million, up \$65.4 million from the prior year, and no short-term debt was outstanding.

While Southland prefers to own the premises from which it conducts its convenience store operations, many desirable locations are available only on a long-term lease basis. The Company considers such leases to be extremely valuable and essential to store expansion. At December 31, 1979, \$208.8 million of capital lease assets were reflected on the balance sheet.

Total capitalization (long-term debt, capital lease obligations, and shareholders' equity) at year-end was \$1.051 billion, compared with \$847.3 million a year earlier. The effect on the Company's capital structure of record 1979 earnings, capital leases, and the equity and long-term debt financing completed during the year is as follows:

CAPITALIZATION (Millions)

Long-Term Debt	\$119.9	\$153.1	\$195.5	\$261.5	\$ 326.9
Capital Lease Obligations	163.4	178.6	192.5	211.3	226.3
Shareholders' Equity	259.9	290.1	330.0	374.5	497.6
TOTAL	\$543.2	\$621.8	\$718.0	\$847.3	\$1,050.8

**PROPERTY, PLANT, AND EQUIPMENT (Including Capital Leases) (Millions)**

\$447.4	\$506.2	\$567.4	\$677.3	\$838.8
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Total Capitalization (Millions)	1979		1978	
	Amount	%	Amount	%
Long-Term Debt	\$ 326.9	31.1	\$261.5	30.9
Capital Lease Obligations	226.3	21.5	211.3	24.9
Shareholders' Equity	497.6	47.4	374.5	44.2
TOTAL	\$1,050.8	100.0	\$847.3	100.0

Capital Investment

Investment in property, plant, and equipment in 1979 totaled \$223.0 million, the largest single-year expenditure program in Southland's history.

Capital outlays for the Stores Group accounted for \$180.9 million, or 81% of total expenditures, principally for new 7-Eleven stores, extensive remodeling of existing facilities and replacement of equipment, self-serve gasoline installations, and sites for additional stores. In addition, the Group's capital spending included expansion and remodeling of facilities at the Florida, Virginia, and Texas Distribution Centers as well as equipment for the new Center in Illinois and the Food Processing Center in Salt Lake City.

Expenditures for the Dairies Group accounted for 5% or \$11.1 million, primarily for the acquisition of Knowlton's dairy, new product capacity, manufacturing and productivity improvement, and vehicles. Capital investments of \$20.3 million, or 9%, for the Special Operations Group included

completion of a new ice processing plant in Dallas and increased capacity at four other facilities, expansion of the Chief Auto Parts Division, remodeling and expansion of Chemical Division facilities, and vehicles for the new distribution center. Corporate capital expenditures were \$10.7 million.

Southland places strong emphasis on ownership of fixed assets and during the past five years has invested over \$600 million in property, plant, and equipment. Reflecting the Company's confidence in the potential of its major business, capital expenditures during this period for store operations and distribution and food processing centers amounted to almost \$550 million, or 90% of the total. Southland's capital spending plans call for continued major investments to strengthen the Company's role in the convenience store business and develop and expand its other operations in line with market opportunities.

Market Data

Southland's common stock is traded under the symbol SLC on the

New York, Pacific, Boston, and Philadelphia Stock Exchanges. The following market price and earnings per share information has been adjusted for a 3% stock dividend in each year. The price/earnings ratios are based upon primary earnings per share for the four preceding quarters.

QUARTER	PRICE RANGE		PRICE/EARNINGS RATIO		
	1979	High	Low	High	Low
First	28½	24¾	9.8	8.4	
Second	28	24⅓	9.8	8.7	
Third	31⅓	26⅓	10.1	8.6	
Fourth	29¾	25¼	9.2	7.8	

1978

	High	Low	High	Low
First	24¼	21⅓	10.5	9.1
Second	28¼	20⅓	11.9	8.8
Third	32¾	24¾	12.8	9.7
Fourth	30	24¼	10.9	8.8

Profit Sharing and Pension Plans

The Company contributes to The Southland Corporation Employees' Savings and Profit Sharing Plan, established in 1949, and to various union pension plans. Eligible employees have the option of joining Southland's voluntary contributory plan. Company contributions to this fully funded, trustee-administered plan are based on pretax earnings. All required contributions to such plans have been made.



The SDC computer-controlled system is designed to meet the unique merchandise requirements of 7-ELEVEN.

Management's Discussion and Analysis of the Consolidated Statement of Earnings

Fiscal Year 1979 Compared with Fiscal Year 1978

At year-end, the Company made three accounting changes (See Note 2 — "Notes to Consolidated Financial Statements") which affected cost of goods sold, interest expense, contribution to profit sharing, and income taxes for the year 1979.

Revenues increased \$786.0 million to \$3.876 billion from \$3.090 billion for 1978. The excellent 25.4% increase reflects primarily the continued popularity of convenience store shopping, effective network television advertising, stepped-up promotional and in-store merchandising programs, a substantial increase in sales of self-serve gasoline, and the opening of new 7-Eleven stores. The Company opened 666 convenience stores and closed 460, for a net gain of 206 stores in 1979, compared with 242 in 1978.

Other income rose from \$13.6 million to \$19.8 million primarily as a result of a substantial increase in interest income from investment of surplus funds, area license royalties, and earnings of affiliates.

Cost of goods sold, including buying and occupancy expenses, for 1979 was up 26.5%, primarily due to the increase in sales and depreciation, rent, and maintenance expenses, which generally rose in proportion to the sales gain. Gross margin for the year declined to 24.59%, compared with 25.21% for 1978, primarily reflecting the adoption of LIFO and the effect of the increase in low-margin gasoline sales as a percentage of the total convenience store product mix, from 13.4% in 1978 to 17.2% in 1979. These factors more than offset the improvement in margins for convenience store merchandise, Dairies Group products, and self-serve gasoline available at 2,107 7-Eleven stores at year-end.

The ratio of expenses (selling, general and administrative expenses,

interest expense, imputed interest expense, and contribution to Employees' Savings and Profit Sharing Plan) to revenues increased to 21.66% from 21.56% for 1978. Selling, general and administrative expenses increased 26.9%, primarily due to increases in advertising, personnel training, labor, and associated payroll costs. Interest expense rose 18.4%, from \$15.8 million to \$18.7 million, primarily reflecting the sale in December, 1978, of \$50 million 9 3/8% debentures, notes issued and assumed in the Chief Auto Parts acquisition, and \$75 million 9 1/2% debentures sold in August, 1979. Imputed interest expense on capital lease obligations increased 11.4% from \$19.3 million in 1978 to \$21.5 million in 1979.

Contributions to the Employees' Savings and Profit Sharing Plan rose 13.7% in 1979 to \$13.3 million, compared with \$11.7 million in 1978, as the result of increased earnings before income taxes.

Income taxes decreased as a result of a reduction in the federal statutory rate and the change in accounting for investment tax credits.

An increase in the ratio of expenses to revenues and lower gross margin resulted in pro forma net return on revenues of 1.76% in 1979, compared with 1.95% in 1978. The cumulative effect of the accounting change for ITC increased net earnings \$15.7 million to \$83.1 million, up 45.5% from 1978 earnings of \$57.1 million.

Fiscal Year 1978 Compared with Fiscal Year 1977

In 1978, revenues increased \$544.7 million to \$3.090 billion, compared with \$2.545 billion for 1977. The excellent 21.4% increase was a result of successful merchandising and advertising programs, gain in average sales volume per store, more aggressive pricing of selected products in convenience stores, a substantial increase in sales of self-serve gasoline, and the opening of new 7-Eleven stores. The Company opened 550 convenience stores and

closed 308, for a net of 242 stores in 1978, compared with 404 in 1977.

Other income rose from \$9,306,000 to \$13,562,000 primarily as a result of a substantial increase in interest income from investment of surplus funds at a higher rate of return, area license royalties, and net gain on sale of assets no longer of use to the Company.

Gross margin for the year was maintained at the 1977 level of 25.21%. A substantial increase in sales of self-serve gasoline, a high-volume, low-margin product available at 1,857 7-Eleven stores at year-end, offset merchandise margin gains in convenience stores and dairies.

The excellent sales gain contributed to a reduction in the ratio of expenses to revenues from 21.67% in 1977 to 21.56% in 1978. Sales increased 21.3%, cost of goods sold, including buying and occupancy expenses, increased 21.4%, and expenses (selling, general and administrative expenses, interest expense, and contribution to Employees' Savings and Profit Sharing Plan) increased 20.8%, compared with 1977. Interest expense rose from \$13,540,000 to \$15,804,000, primarily as a result of the \$50 million 8 3/8% debentures sold in March, 1977, and mortgage debt incurred to finance new 7-Eleven stores. Imputed interest expense on capital lease obligations, accounted for in accordance with SFAS 13, increased from \$18,064,000 in 1977 to \$19,325,000 in 1978.

Contributions to the Employees' Savings and Profit Sharing Plan rose 20.4% in 1978 to \$11.7 million, compared with \$9.7 million in 1977, as the result of increased earnings before income taxes.

A reduction in the ratio of expenses to revenues resulted in net return on revenues of 1.85%, compared with 1.78% for 1977. Net earnings were a record \$57.1 million, up 26.0% from 1977 earnings of \$45.3 million.

Business Segment Information

Revenues by business segment include net sales to outside customers and other income, principally interest earned from the investment of surplus funds, area license royalties, earnings

of affiliates, and net gain on sale of assets no longer of use to the Company. Operating profits represent total revenues less operating expenses before interest costs and unallocated corporate expense.

						Years Ended December 31				
(Millions)	1979		1978		1977		1976		1975	
Revenues:										
Stores Group	\$3,463.6	89%	\$2,791.0	90%	\$2,271.9	89%	\$1,857.5	88%	\$1,556.0	87%
Dairies Group	314.7	8	253.4	8	236.5	9	236.1	11	208.3	12
Special Operations Group	90.7	3	40.9	2	33.7	2	26.0	1	25.0	1
Corporate	7.0	—	4.8	—	3.3	—	2.4	—	1.5	—
TOTAL	\$3,876.0	100%	\$3,090.1	100%	\$2,545.4	100%	\$2,122.0	100%	\$1,790.8	100%
Operating Profits:										
Stores Group	\$ 145.8	89%	\$ 142.7	92%	\$ 115.7	90%	\$ 92.3	86%	\$ 80.8	88%
Dairies Group	10.3	6	6.7	4	6.0	5	8.6	8	10.1	11
Special Operations Group	7.6	5	6.0	4	6.7	5	6.4	6	0.9	1
TOTAL	\$ 163.7	100%	\$ 155.4	100%	\$ 128.4	100%	\$ 107.3	100%	\$ 91.8	100%

Supplemental Information — The Impact of General Inflation on Selected Financial Data

General

The Financial Accounting Standards Board recently issued Statement of Financial Accounting Standards No. 33, which provides for two supplementary methods of income computation to present information designed to reflect the impact of inflation on major public companies. The first (constant dollar method) adjusts for the effects of general inflation and the second (current cost method) for the effects of changes in specific prices on inventories, property, plant, and equipment, capital leases, cost of sales, and depreciation and amortization.

Because there are differences of opinion as to which method, if either, best presents the impact of inflation, and the Company believes that there will be certain refinements to the current cost method, it has elected to defer reporting on that basis until the end of 1980.

The following constant dollar information, which is based on average 1979 dollars, is presented as an experiment and should be viewed as such, as it inherently involves the use of assumptions, approximations, and estimates.

Statements of Net Earnings and Changes in Shareholders' Equity
Cost of goods sold and depreciation and amortization have been adjusted

for the effects of general inflation in order to compute net earnings. The Consumer Price Index for all Urban Consumers has been used to restate selected information to match net revenues with certain expenses in dollars of equivalent purchasing power (constant dollars). Net revenues, other operating expenses, and interest expense are assumed to be in constant dollars and, accordingly, have not been adjusted.

The Company's historical cost of net property, plant, and equipment has been increased \$207.4 million to reflect replacement cost in constant dollars. Earnings are reduced by the resulting adjustment to depreciation and amortization.



Automated equipment improves productivity and assures fine quality dairy products.

The adjustment to cost of goods sold is minimal since the LIFO inventory method closely approximates cost of sales, adjusted for general inflation. However, during inflationary times, LIFO tends to undervalue inventories; therefore, inventories were increased \$9.1 million to reflect constant dollars.

Although the adjustments to cost of goods sold and depreciation and amortization lower earnings, companies are not permitted to reduce income taxes for general inflation adjustments.

Changes in shareholders' equity includes additional information on the effect of inflation — "unrealized gain from decline in purchasing power of net amounts owed." This amount is determined by calculating net monetary liabilities (amounts owed, less cash and other claims to cash, stated in fixed dollars) at the beginning and end of the year, adjusted for changes during the year, stated in constant dollars. As the Company incurred net monetary liabilities during a period of inflation, there was an unrealized gain.

	Year Ended December 31, 1979	
	As reported in financial statements	Adjusted for general inflation
Net revenues	\$3,876.0	\$3,876.0
Cost of sales and expenses:		
Cost of goods sold, exclusive of depreciation and amortization	2,821.6	2,825.6
Depreciation and amortization	79.1	99.1
Other operating expenses	821.7	821.7
Interest expense including imputed interest expense on capital lease obligations	40.2	40.2
Earnings before income taxes	113.4	89.4
Income taxes	46.1	46.1
Earnings before cumulative effect of accounting change for investment tax credits	67.3	43.3
Cumulative effect of accounting change for investment tax credits	15.7	15.7
Net earnings	\$ 83.0	\$ 59.0
Pro forma earnings, with accounting change for investment tax credits applied retroactively	\$ 68.3	\$ 44.3
Unrealized gain from decline in purchasing power of net amounts owed	\$ —	\$ 78.8
Changes in shareholders' equity:		
Shareholders' equity, beginning of year	\$ 374.6	\$ 573.3
Net earnings	83.0	59.0
Unrealized gain from decline in purchasing power of net amounts owed	—	78.8
Sale of additional common shares	55.9	55.9
Other changes	(15.9)	(15.9)
Shareholders' equity, end of year	\$ 497.6	\$ 751.1

Five-Year Table of Selected Financial Data

The following comparison shows the effects of adjusting certain historical financial information to constant dollars.

(Millions, except per share data)	1975	1976	1977	1978	Years Ended December 31 1979
Net revenues	\$2,415.8	\$2,705.6	\$3,049.4	\$3,439.3	\$3,876.0
Pro forma net earnings *					44.3
Per share data:					
Pro forma primary earnings *					2.04
Pro forma earnings assuming full dilution *					1.99
Market price at year-end	29	34 $\frac{5}{8}$	31 $\frac{3}{8}$	31 $\frac{1}{4}$	28 $\frac{3}{4}$
Cash dividends	9.5	11.0	13.1	15.2	17.5
Average consumer price index	161.2	170.5	181.5	195.4	217.4

* Pro forma amounts reflect the accounting change for investment tax credits.

CONSOLIDATED STATEMENTS OF EARNINGS

THE SOUTHLAND CORPORATION AND SUBSIDIARIES

Years ended December 31 (Dollars in thousands except per share data)

	1979	1978	1977	1976	1975
Revenues:					
Net sales	\$3,856,222	\$3,076,532	\$2,536,109	\$2,115,769	\$1,787,928
Other income	19,837	13,562	9,306	6,254	2,877
	3,876,059	3,090,094	2,545,415	2,122,023	1,790,805
Cost of Sales and Expenses (Note 2):					
Cost of goods sold, including buying and occupancy expenses	2,922,982	2,311,024	1,903,791	1,577,141	1,323,799
Selling, general, and administrative expenses	785,979	619,519	510,337	435,687	374,234
Interest expense	18,746	15,804	13,540	9,707	7,936
Imputed interest expense on capital lease obligations	21,490	19,325	18,064	15,388	13,969
Contributions to Employees' Savings and Profit Sharing Plan	13,304	11,714	9,726	8,346	6,995
	3,762,501	2,977,386	2,455,458	2,046,269	1,726,933
Earnings Before Income Taxes	113,558*	112,708	89,957	75,754	63,872
Income Taxes (Notes 2, 7, and 10)	46,082*	55,611	44,640	37,905	31,804
Earnings Before Cumulative Effect of accounting change for investment tax credits	67,476	57,097	45,317	37,849	32,068
Cumulative Effect of accounting change for investment tax credits (Note 2)	15,665	—	—	—	—
Net Earnings	\$ 83,141	\$ 57,097	\$ 45,317	\$ 37,849	\$ 32,068
Earnings Per Share (Notes 2 and 11):					
Earnings before cumulative effect of accounting change:					
Primary	\$3.12	\$2.75	\$2.20	\$1.86	\$1.58
Fully diluted	\$3.02	\$2.66	\$2.13	\$1.80	\$1.53
Net earnings:					
Primary	\$3.84	\$2.75	\$2.20	\$1.86	\$1.58
Fully diluted	\$3.72	\$2.66	\$2.13	\$1.80	\$1.53
Pro Forma Earnings, with accounting change for investment tax credits applied retroactively (Note 2):	\$ 68,273	\$ 60,357	\$ 47,664	\$ 40,037	\$ 33,717
Pro Forma Earnings Per Share (Note 2):					
Primary	\$3.16	\$2.90	\$2.31	\$1.97	\$1.67
Fully diluted	\$3.06	\$2.81	\$2.24	\$1.90	\$1.61

* Includes current year effect of accounting changes.
See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS
THE SOUTHLAND CORPORATION AND SUBSIDIARIES

ASSETS

	December 31	December 31
	1979	1978
Current Assets:		
Cash and short-term investments (Note 3)	\$ 79,927,065	\$ 82,745,504
Accounts and notes receivable (Note 4)	96,383,120	68,744,325
Inventories (Note 2)	200,793,642	171,478,745
Deposits and prepaid expenses (Note 7)	30,507,890	24,777,392
Investment in properties	67,500,000	55,857,419
Total Current Assets	475,111,717	403,603,385
Investments in Affiliates (Note 1)	28,847,437	27,364,352
Property, Plant, and Equipment (Notes 2 and 5)	630,025,503	479,554,364
Capital Leases (Note 9)	208,770,246	197,730,040
Other Assets	24,819,962	26,223,652
	\$1,367,574,865	\$1,134,475,793

LIABILITIES AND SHAREHOLDERS' EQUITY

Current Liabilities:		
Accounts payable and accrued expenses	\$ 275,512,771	\$ 211,920,848
Income taxes	6,626,199	18,636,987
Long-term debt due within one year (Note 6)	4,024,901	13,254,868
Capital lease obligations due within one year (Note 9)	20,361,947	20,157,217
Total Current Liabilities	306,525,818	263,969,920
Deferred Credits (Notes 2 and 7)	10,293,951	23,235,908
Long-Term Debt (Note 6)	326,892,766	261,460,472
Capital Lease Obligations (Note 9)	226,257,199	211,342,074
Commitments for Operating Leases (Note 9)		
Shareholders' Equity (Notes 6 and 8):		
Common stock, \$.01 par value, authorized 40,000,000 shares, issued and outstanding 22,935,504 and 20,200,557 shares	229,355	202,006
Additional capital	319,067,335	242,339,822
Retained earnings	178,308,441	131,925,591
	497,605,131	374,467,419
	\$1,367,574,865	\$1,134,475,793

See notes to consolidated financial statements.

The Dairies
Group spon-
sored nation-
wide the
“Mothers March
on Birth
Defects.”



**CONSOLIDATED STATEMENTS
OF SHAREHOLDERS' EQUITY**
THE SOUTHLAND CORPORATION AND SUBSIDIARIES

	Year ended December 31	
	1979	1978
Common Stock:		
Balance, beginning of year	\$ 202,006	\$ 195,573
Sale of stock	20,000	—
3% Stock dividend	6,642	5,842
Key employees incentive plan	303	195
Conversion of notes	214	—
Acquisition	180	—
Employee stock options	10	396
Balance, end of year	229,355	202,006
Additional Capital:		
Balance, beginning of year	242,339,822	223,499,143
Sale of stock	55,907,632	—
3% Stock dividend	19,255,100	17,665,815
Key employees incentive plan	788,563	470,797
Conversion of notes	269,786	—
Acquisition	476,237	—
Employee stock options	30,195	704,067
Balance, end of year	319,067,335	242,339,822
Retained Earnings:		
Balance, beginning of year	131,925,591	106,257,781
Net earnings for the year	83,140,568	57,097,109
Cash dividends	(17,381,682)	(13,627,443)
3% Stock dividend	(19,261,742)	(17,671,657)
Cash paid in lieu of fractional shares on stock dividend	(114,294)	(130,199)
Balance, end of year	178,308,441	131,925,591
Total Shareholders' Equity	\$497,605,131	\$374,467,419

See notes to consolidated financial statements.



Southland raised a record \$4.23 million in contributions for the Muscular Dystrophy Association and "Jerry's Kids."

**CONSOLIDATED STATEMENTS OF
CHANGES IN FINANCIAL POSITION**
THE SOUTHLAND CORPORATION AND SUBSIDIARIES

Sources of Working Capital:	Year ended December 31	
	1979	1978
From operations:		
Net earnings	\$ 83,140,568	\$ 57,097,109
Expenses charged to earnings which did not require outlay of working capital:		
Depreciation and amortization	56,501,186	46,839,875
Amortization of capital leases	22,609,981	20,884,330
Deferred income taxes and other credits	(12,948,857)	6,552,597
Working capital provided from operations	149,302,878	131,373,911
Long-term debt	78,858,875	70,658,506
Capital lease obligations	38,269,067	41,907,748
Retirements and sales of property	16,031,704	13,555,200
Retirements and sales of capital leases	11,318,749	1,397,049
Other	1,737,017	(366,089)
Issuance of common stock:		
Sale of stock	55,927,632	—
Key employees incentive plan	788,866	470,992
Conversion of notes	270,000	—
Acquisition	476,417	—
Employee stock options	30,205	704,463
	353,011,410	259,701,780
Uses of Working Capital:		
Property, plant, and equipment	217,087,139	141,438,084
Capital leases	38,269,067	41,907,748
Reduction of capital lease obligations	30,053,811	23,112,351
Payment of long-term debt	13,268,113	4,718,034
Cash dividends	17,381,682	13,627,443
Net noncurrent assets of businesses purchased for stock and cash	6,131,785	29,180,394
Retirement of long-term debt upon conversion of notes	270,000	—
Investments in affiliates	1,483,085	647,216
Cash paid in lieu of fractional shares on stock dividend	114,294	130,199
	324,058,976	254,761,469
Increase in working capital	\$ 28,952,434	\$ 4,940,311
Changes in Working Capital:		
Increases (decreases) in current assets:		
Cash and short-term investments	\$ (2,818,439)	\$ 16,841,703
Accounts and notes receivable	27,638,795	3,516,525
Inventories	29,314,897	34,621,589
Deposits and prepaid expenses	5,730,498	5,340,768
Investment in properties	11,642,581	2,537,927
	71,508,332	62,858,512
Increases (decreases) in current liabilities:		
Accounts payable and accrued expenses	63,591,923	43,026,457
Income taxes	(12,010,788)	3,155,570
Long-term debt due within one year	(9,229,967)	9,112,813
Capital lease obligations due within one year	204,730	2,623,361
	42,555,898	57,918,201
Increase in working capital	\$ 28,952,434	\$ 4,940,311

See notes to consolidated financial statements.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 1979 AND 1978
THE SOUTHLAND CORPORATION AND SUBSIDIARIES**

1. Accounting Policies:

Principles of Consolidation

The financial statements include the accounts of domestic and Canadian subsidiaries, all of which are wholly-owned. Intercompany transactions are eliminated.

Investments in affiliates are accounted for by the equity method. Accordingly, such investments are shown at cost to the Company plus equity in undistributed earnings since acquisition. Equity in earnings of affiliates is included in other income. Investments in affiliates consists primarily of amounts invested in a wholly-owned United Kingdom subsidiary engaged in the operation of retail stores. Equity in earnings of foreign affiliates is recorded net of amortization of the intangibles which arose on the acquisition (straight-line over 40 years), foreign income taxes, and a provision for United States federal income taxes.

The classifications in use for the current year have been applied to the statements for 1978.

Revenues

Net sales are comprised of sales of products and merchandise (including sales by stores operated by franchisees) and other operating revenues.

Sales by stores operated under domestic and foreign area license agreements are not included. All fees or royalties arising from such agreements are included in other income. Initial fees are recognized as

the services required under the agreements are performed.

Inventories

Inventories are stated at the lower of cost or market, which, as to merchandise in stores, is determined by the retail inventory method. In 1978, cost was determined using the first-in, first-out (FIFO) method. Beginning in 1979, the Company adopted the last-in, first-out (LIFO) method of determining the cost of substantially all inventories of the Stores Group. The cost of all other inventories is determined using the FIFO method.

Investment in Properties

Investment in properties includes land, buildings, and equipment either to be sold for cash and leased back or to be mortgaged, as well as closed stores held for sale. The Company expects that cash will be realized for these properties within a twelve-month period. Working capital is used in the acquisition, construction, and carrying of these assets.

Depreciation and Amortization

Depreciation of plant and equipment and amortization of capital leases is based upon the estimated useful lives of these assets using the straight-line method. Amortization of improvements to leased properties is based upon the remaining terms of the leases or the estimated useful lives of such improvements, whichever is shorter.

Interest

Interest is expensed currently, except for interest incurred to finance the construction or development of properties, which, beginning in 1979, has been added to the cost of the asset.

Income Taxes and Investment Tax Credits

In 1978 and prior years, investment tax credits relating to leased and purchased equipment were deferred and taken into income ratably over either the terms of the leases or the useful lives of the assets. Beginning in 1979, investment tax credits reduce income taxes in the year the related assets are placed in service.

The tax effects of differences in timing between financial and tax reporting have been provided for in the financial statements. The resulting deferred taxes arise principally from the use of accelerated depreciation methods for tax purposes and the capitalization of leases and certain interest, as well as a provision for insurance claims, for financial statement purposes.

Leases

Capital leases are recorded at the lower of the discounted present value of future lease payments or the fair value of the property. Provision is made for the present value of estimated losses anticipated to be incurred due to the payment of rentals on closed stores, net of expected sublease rentals.



Conveniently packaged "Reddy Ice" is available at many 7-ELEVEN stores.

2. Accounting Changes:

Inventories

In 1979, the Company changed from the FIFO to the LIFO method of determining the cost of substantially all inventories of the Stores Group. At December 31, 1978, all inventories were stated at FIFO cost. At December 31, 1979, inventories stated on the LIFO basis were approximately \$150,426,000, which is less than replacement cost by approximately \$21,160,000. The effect of this change was to reduce net earnings for 1979 by approximately \$8,613,000, or \$.40 per share (primary). This change was made because management believes the LIFO method more realistically reflects earnings during inflationary periods by matching the most recent inventory acquisition costs against current sales.

It is not possible to restate prior years' reported earnings, or to determine the cumulative effect of the change to LIFO on retained earnings at Jan-

uary 1, 1979. Therefore, the current year's financial statements are not comparable with those of any prior year.

Capitalization of Interest

In 1979, the Company adopted Statement of Financial Accounting Standards No. 34, which requires that interest incurred to finance the construction or development of properties be added to the cost of the asset. Accordingly, in 1979 the Company capitalized \$4,387,740 of such interest. The effect of this change was to increase net earnings for 1979 by approximately \$2,010,000, or \$.09 per share (primary).

Investment Tax Credits

In 1979, the Company changed from the deferral to the flow-through method of accounting for investment tax credits. This change makes the Company's method of accounting for investment tax credits comparable with most other retailers and eliminates

the future effects of continuing inflation on these credits. The effect of this change was to: (a) increase 1979 net earnings for credits earned during 1979 by approximately \$6,603,000, or \$.31 per share (primary), which reduced income taxes in the 1979 consolidated statement of earnings; (b) increase 1979 net earnings for net credits previously deferred, included in the balance sheet as deferred credits at December 31, 1978, by \$15,664,697, or \$.72 per share (primary), which has been retroactively reflected in 1979 first quarter results as the cumulative effect of accounting change for investment tax credits; and (c) decrease 1979 net earnings for the additional contribution to the Employees' Savings and Profit Sharing Plan resulting from (b) above, net of tax benefit, by approximately \$797,000, or \$.04 per share (primary), which has been retroactively reflected in 1979 first quarter results. Cash flow was not affected by (a) and (b) above.

3. Cash and Short-Term Investments:

Cash and short-term investments include certificates of deposit, commercial paper, and U.S. Treasury Notes of \$77,252,792 and \$78,156,064 at December 31, 1979 and 1978, respectively. These short-term investments are stated at cost, which approximates market.

4. Accounts and Notes Receivable:

	1979	1978
Trade	\$79,025,537	\$51,492,239
Franchisee	21,744,376	20,020,022
	100,769,913	71,512,261
Allowance for doubtful accounts	(4,386,793)	(2,767,936)
	\$96,383,120	\$68,744,325

5. Property, Plant, and Equipment:

Approximately 19% of the carrying amount of property, plant, and equipment is mortgaged. Lenders to certain wholly-owned real estate subsidiaries hold pledges of the shares of those subsidiaries as additional collateral.

	1979	1978
COST:		
Land	\$ 99,669,680	\$ 71,690,295
Buildings and leaseholds	307,827,238	268,581,812
Machinery and equipment	365,755,554	282,740,267
Vehicles	69,107,677	57,434,478
Construction in process	38,752,489	15,338,026
	881,112,638	695,784,878
Accumulated depreciation and amortization	(251,087,135)	(216,230,514)
	\$630,025,503	\$479,554,364

6. Long-Term Debt:

At December 31, 1979, long-term debt and amounts due within one year were as follows:

	Amount outstanding	Due within one year	Balance included in long-term debt
5%-9.88% Real estate, equipment, and other notes (mature 1980 to 2007)	\$117,842,550	\$4,024,901	\$113,817,649
5% Convertible sub-ordinated debentures due 1987	30,000,000	—	30,000,000
8½% Sinking fund debentures due 2002	50,000,000	—	50,000,000
9¾% Sinking fund debentures due 2003	49,876,437	—	49,876,437
9½% Sinking fund debentures due 2004	73,198,680	—	73,198,680
16% Note issued in acquisition (payable 1981)	10,000,000	—	10,000,000
	\$330,917,667	\$4,024,901	\$326,892,766

The 5% convertible debentures may, at the option of the holders, be converted at any time prior to maturity into the Company's common stock. The present conversion ratio is 29.26 shares for each \$1,000 of principal. At December 31, 1979, there were 877,800 shares reserved for the conversion of these debentures.

The 8½% debentures require annual sinking fund payments beginning February 15, 1983, in the amount of \$2,500,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding \$2,500,000.

The 9¾% debentures require annual sinking fund payments beginning December 15, 1984, in the

amount of \$2,500,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding \$2,500,000.

The 9½% debentures require annual sinking fund payments beginning August 15, 1985, in the amount of \$3,750,000, which, at the option of the Company, may be increased each year by an additional amount not exceeding \$5,625,000.

At December 31, 1979, the aggregate amounts of long-term debt maturities were as follows for the years ending December 31: 1980 — \$4,025,000; 1981 — \$14,213,000; 1982 — \$4,210,000; 1983 — \$4,503,000; 1984 — \$4,560,000.

7. Deferred Credits:

Deferred credits include deferred federal income taxes of \$9,225,241 and \$5,762,608 at December 31, 1979 and 1978, respectively, and \$15,664,697 of deferred investment tax credits at December 31, 1978. The net current asset portion of deferred

income taxes of \$8,784,399 and \$5,984,342 at December 31, 1979 and 1978, respectively, were included in deposits and prepaid expenses. Investment tax credits included in income were \$9,427,530 in 1979 and \$2,409,971 in 1978.

8. Common Stock:

At December 31, 1979, under a nonqualified stock option plan, options for 233,249 shares were outstanding at prices ranging from \$19.67 to \$26.94 per share, of which options for 63,171 shares were exercisable. During 1979, an option for 2,575 shares was granted at \$26.94 per share, and options for 1,077 shares were exercised at \$19.67 and \$23.33 per share. During 1978, options for 26,522 shares were granted at \$23.33 per share, options for 4,223 shares were exercised at prices ranging from \$19.67 to \$23.33, and options for 5,464 shares expired or were cancelled. At December 31, 1979, an additional 307,786 shares were available for future grants under this plan. Options are granted at the fair market value of the shares on date of grant and are exercisable ratably over a ten-year period. The proceeds from shares issued and any applicable tax benefits related to these options are credited to common stock and additional capital. No charges or credits are made to income with regard to options granted under this plan.

At December 31, 1979, 28,587 shares were reserved for issuance pursuant to a key employees incentive plan, of which approximately 20,000 shares will be issued in 1980. In 1979 and 1978, respectively, 31,251 and 20,712 shares were issued under this plan.

Under a terminated qualified stock option plan, 37,739 shares were issued during 1978 at prices ranging from \$15.86 to \$18.33 per share and all remaining options expired or were cancelled. No charges or credits were made to income with regard to options granted under this plan.

The above information has been adjusted for stock dividends.

9. Leases:

Certain of the property and equipment used in the Company's business is leased. Generally, real estate leases are for primary terms of from 14 to 20 years with options to renew for additional periods, and equipment

leases are for terms of from 5 to 10 years. The leases do not contain restrictions which have a material effect on the Company's operations.

The composition of capital leases reflected as assets in the consolidated balance sheets is as follows:

	1979	1978
Buildings	\$260,528,230	\$240,863,258
Equipment	102,434,997	98,523,728
	362,963,227	339,386,986
Accumulated amortization	(154,192,981)	(141,656,946)
	\$208,770,246	\$197,730,040

Capital Lease Obligations

The present value of minimum lease payments for capital lease obligations of \$246,619,146 at December 31, 1979, is reflected in the consolidated balance sheet as current and noncurrent capital lease obligations of \$20,361,947 and \$226,257,199, respectively, and represents the total minimum lease payments less estimated executory costs of \$12,796,339 and an amount representing imputed interest of \$179,725,702. Future minimum lease payments on these leases totaled \$439,141,000 and are due in: 1980 —

\$42,655,000; 1981 — \$39,539,000; 1982 — \$36,643,000; 1983 — \$33,172,000; 1984 — \$31,062,000; and thereafter — \$256,070,000.

The amount representing imputed interest necessary to reduce net minimum lease payments to present value has been calculated generally at the Company's incremental borrowing rate at the inception of each lease. Noncancelable sublease rental income and contingent rental expense are not material and have not been reflected in total minimum lease payments.

Operating Leases

Future minimum lease payments required by operating leases at December 31, 1979, totaled \$336,822,000 and are due in: 1980 — \$33,493,000; 1981 — \$30,991,000; 1982 — \$28,425,000; 1983 — \$26,322,000; 1984 — \$23,764,000; and thereafter — \$193,827,000. These lease payments have not been reduced by \$3,161,000 of future rental income under noncancelable subleases.

Lease expense on operating leases in the years ended December 31, 1979 and 1978, totaled \$36,961,000 and \$28,617,000, respectively. Contingent rental expense is not material.

Leases With Profit Sharing

During 1979, The Southland Corporation Employees' Savings and Profit Sharing Plan (Profit Sharing) purchased 125 7-Eleven stores from the Company for \$26,606,465, the Company's direct cost plus 15% which approximates expenses incurred. The stores were simultaneously leased to the Company at annual rentals approximating market rates. At December 31, 1979, Profit Sharing owned 1,056 stores leased to the Company under capital leases, which are reflected in buildings in the table above at a carrying amount of \$56,591,000, and 106 stores leased to the Company under operating leases.

10. Income Taxes:

Provisions for income taxes are as follows:

	1979	1978
Federal:		
Current	\$39,048,000	\$44,564,000
Deferred	241,000	5,121,000
State	6,793,000	5,926,000
	\$46,082,000	\$55,611,000

A reconciliation of the Company's effective tax rate and the federal statutory rate is as follows:

	1979	1978
Statutory rate	46.0%	48.0%
Investment tax credits	(8.3)	(1.0)
State income taxes net of federal income tax benefit	3.2	2.7
Other	(.3)	(.4)
	40.6%	49.3%

11. Earnings Per Share:

Primary earnings per share are based upon the average number of shares outstanding during each year after giving effect to subsequent stock dividends.

Earnings per share assuming full dilution are based on (a) the number of shares used in computing primary earnings per share, (b) shares issuable upon conversion of convertible notes and debentures at the stated conversion rates (related interest requirements eliminated), (c) the number of shares issuable on the exercise of stock options after reduction for shares assumed to have been purchased with the proceeds, and (d) average shares issuable under the key employees incentive plan.

12. Pro Forma Quarterly Financial Data (Unaudited):

Data reflected for the 1979 quarterly periods is not comparable to the 1978 quarterly data as a result of the adoption of the LIFO inventory method and the capitalization of certain interest.

Previously reported 1979 quarterly information included in the following table has been restated to give pro forma effect to the accounting changes described in Note 2. The 1978 information gives pro forma effect only to the accounting change for investment tax credits.

The classification of items in determining gross profit conforms to that used in the consolidated statements of earnings. Summarized quarterly financial data is as follows (000's omitted, except per share data):

		Net Sales	Gross Profit	Net Earnings	Earnings per share Primary	Fully Diluted
1979:						
First quarter	\$ 807,372	\$186,515	\$ 6,768	\$.33	\$.32	
Second quarter	956,301	245,621	23,494	1.12	1.09	
Third quarter	1,053,851	263,384	24,535	1.14	1.09	
Fourth quarter	1,038,698	237,720	13,476	.57	.56	
Year	\$3,856,222	\$933,240	\$68,273	\$3.16	\$3.06	
1978:						
First quarter	\$ 646,083	\$155,270	\$ 7,461	\$.36	\$.35	
Second quarter	774,465	198,804	19,071	.92	.89	
Third quarter	844,521	210,748	19,992	.96	.93	
Fourth quarter	811,463	198,623	13,833	.66	.64	
Year	\$3,076,532	\$763,445	\$60,357	\$2.90	\$2.81	

13. Replacement Cost Information (Unaudited):

Estimated replacement cost information for inventories and productive assets and the related effect on cost of goods sold and depreciation expense will appear in the Company's annual report on Form 10-K to be filed with the Securities and Exchange Commission.

Generally, this information will indicate that replacing productive assets with others having equivalent productive capacity would require a

substantially greater investment than when originally purchased, primarily reflecting the cumulative effect of price changes on these assets. The replacement cost of inventories would be significantly greater at December 31, 1979, because in 1979 the Company adopted the LIFO inventory method for substantially all of its inventories. Cost of goods sold would be greater in 1979 and 1978 due to the incremental depreciation associated with the higher replacement cost of gross productive assets and, in 1978, also due

to increases in the unit cost of merchandise purchased for sale. Beginning in 1979, excluding depreciation and amortization expense, cost of goods sold approximates replacement cost as a result of the use of the LIFO inventory method.

Since the Company has been able to react quickly to cost changes and make appropriate adjustments to selling prices, it has been able to mitigate the effect of these cost increases on operations.

The 7-ELEVEN
"Submarine" sandwich was a
winner on
network TV.



14. Segment Information:

The Stores Group includes all convenience and grocery stores in the United States and Canada, as well as those activities (such as self-serve gasoline, distribution, and food preparation) which derive the majority of their revenues and operating profits from support of these stores. The Dairies Group includes milk and ice cream processing and distribution, salad-making, and packaging. The Special Operations Group includes the ice, chemical, truck leasing, and retail auto parts divisions. Corporate items reflect income, expenses, and assets not allocable to segments.

Intersegment sales are accounted for on a cost plus markup basis. Expenses directly identifiable with a segment and certain allocated expenses are used to determine operating profit by segment.

The 1978 information is shown on a pro forma basis to reflect retroactively the accounting change for investment tax credits. The operating profits of the Stores Group was reduced in 1979 by approximately \$16,920,000 as a result of the adoption of the LIFO inventory method.

(000's Omitted)	1979	1978
Revenues:		
Stores Group	\$3,463,614	\$2,791,035
Dairies Group	473,367	388,956
Special Operations Group	113,919	56,161
Corporate	6,968	4,801
	4,057,868	3,240,953
Intersegment revenues:		
Dairies Group	(158,622)	(135,563)
Special Operations Group	(23,187)	(15,296)
Consolidated revenues	\$3,876,059	\$3,090,094
Operating profits:		
Stores Group	\$ 145,831	\$ 141,208
Dairies Group	10,326	6,433
Special Operations Group	7,579	5,668
Consolidated operating profits	163,736	153,309
Interest expense	(40,236)	(35,129)
Corporate expense — net	(9,942)	(7,641)
Consolidated earnings before income taxes	\$ 113,558	\$ 110,539
Identifiable assets (including capital leases) at December 31:		
Stores Group	\$1,045,898	\$ 863,228
Dairies Group	112,854	100,265
Special Operations Group	108,744	80,206
Corporate	100,079	90,777
Total identifiable assets	\$1,367,575	\$1,134,476
Capital expenditures (excluding capital leases):		
Stores Group	\$ 180,950	\$ 110,508
Dairies Group	11,126	9,710
Special Operations Group	20,269	23,054
Corporate	10,659	9,116
	\$ 223,004	\$ 152,388
Depreciation and amortization expense:		
Stores Group	\$ 60,822	\$ 53,572
Dairies Group	7,060	5,737
Special Operations Group	8,571	7,961
Corporate	2,658	2,864
	\$ 79,111	\$ 70,134

The new
“Naturally Yours”
yogurts are
customer favorites.



Management's Responsibility for Financial Reporting

The consolidated financial statements of The Southland Corporation and Subsidiaries, as well as other financial information contained in this report, were prepared by management, which is responsible for their integrity and objectivity.

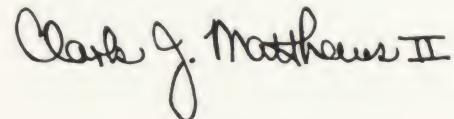
The Company's financial position and results of operations are presented in conformity with generally accepted accounting principles and, where appropriate, reflect estimates based on judgments of management. The Company has designed and implemented accounting and reporting systems and controls to provide reasonable assurance that transactions are accurately reflected on the books and records, assets are protected, established policies and procedures are followed, and the Company's financial position and results of operations are presented fairly. Accounting and reporting controls are monitored through an

extensive program of internal audits by a professional staff of Company auditors which coordinates its activities with the Company's independent certified public accountants.

Touche Ross & Co. is engaged to examine the consolidated financial statements and issue reports thereon. Their examination is conducted in accordance with generally accepted auditing standards, including a review of internal controls and such tests of the accounting records as they consider necessary.

The Board of Directors, assisted by its Audit Committee of four non-employee directors, is responsible for assuring that management fulfills its responsibilities in the preparation of the financial statements and for recommending to shareholders the engagement of the independent certified public accountants, with whom the Committee reviews the scope of the audit and the accounting principles to be applied in financial reporting. The committee meets as

necessary, but at least three times a year. Touche Ross & Co. and the Company's auditors have direct access to the Committee — with or without the presence of management — to discuss any appropriate matter.



Clark J. Matthews, II
Executive Vice President
and Chief Financial Officer

TOUCHE ROSS & CO.

2001 BRYAN TOWER, SUITE 2400
DALLAS, TEXAS 75201

Board of Directors and Shareholders
The Southland Corporation
Dallas, Texas

We have examined the consolidated balance sheets of The Southland Corporation and subsidiaries as of December 31, 1979 and 1978, and the related consolidated statements of earnings, shareholders' equity, and changes in financial position for the

years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of The Southland Corporation and subsidiaries at December 31, 1979 and 1978, and the results of their operations and the changes in their financial position for the years then

ended, in conformity with generally accepted accounting principles consistently applied during the periods except for the accounting changes, with which we concur, described in Note 2 to the consolidated financial statements.



Certified Public Accountants

Dallas, Texas
February 11, 1980

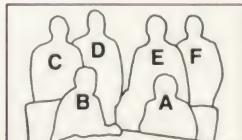


7-ELEVEN satisfies team-size appetites.

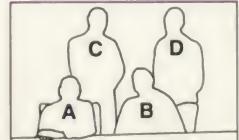


BOARD OF DIRECTORS

- A. JOHN P. THOMPSON (1948)
Chairman of the Board and
Chief Executive Officer
- B. JERE W. THOMPSON (1961)
President
- C. WALTON GRAYSON, III (1962)
Executive Vice President
- D. JOSEPH S. HARDIN (1977)
Executive Vice President
- E. J. C. THOMPSON, JR. (1979)
Executive Vice President
- F. CLIFFORD W. WHEELER (1960)
Retired Vice President



- A. J. Y. BALLARD* (1937)
Consulting Engineer
- B. WILLIAM W. ATWELL* (1976)
Investments
- C. ALAN C. SCHOELLKOPF* (1979)
Vice President,
Rotan Mosle Inc.
- D. MARK L. LEMMON, M.D.* (1977)
Plastic and Reconstructive Surgeon



(Date indicates year elected)
*Members of Audit Committee

OFFICERS

JOHN P. THOMPSON 54
Chairman of the Board and
Chief Executive Officer

JERE W. THOMPSON 47
President

WALTON GRAYSON, III 51
Executive Vice President,
Administration and Services

JOSEPH S. HARDIN 64
Executive Vice President,
Planning and Special Operations Group

CLARK J. MATTHEWS, II 43
Executive Vice President and
Chief Financial Officer

J. C. THOMPSON, JR. 39
Executive Vice President, Retail

RAY D. BERRY 39
Vice President, Stores Group

M. T. COCHRAN, JR. 61
Vice President

S. R. DOLE 42
Vice President, Stores Group

JOSEPH S. HARDIN, JR. 34
Vice President,
Planning and Special Operations Group

VAUGHN R. HEADY 59
Vice President

JAMES W. PARKER 41
Vice President, Dairies Group

W. K. RUPPENKAMP 60
Vice President, Financial Relations

FORREST STOUT 61
Vice President

R G SMITH 56
Secretary and Treasurer

P. EUGENE PENDER 48
Controller

SHAREHOLDERS INFORMATION

SECURITIES LISTED:

COMMON STOCK

8 1/2% SINKING FUND DEBENTURES

9 1/2% SINKING FUND DEBENTURES

9 1/2% SINKING FUND DEBENTURES

New York Stock Exchange

5% CONVERTIBLE SUBORDINATED
DEBENTURES

Luxembourg Stock Exchange

TRANSFER AGENT AND REGISTRAR:

COMMON STOCK

First National Bank in Dallas

8 1/2% SINKING FUND DEBENTURES

Mercantile National Bank at Dallas

9 1/2% SINKING FUND DEBENTURES

9 1/2% SINKING FUND DEBENTURES

First International

Bank in Houston, N.A.

AUDITORS:

Touche Ross & Co.

Dallas, Texas

ANNUAL MEETING:

The Annual Meeting of the Company will be held at 10 a.m. Wednesday, April 23, 1980, in the North Wing Auditorium of the Corporate Office, 2828 North Haskell Avenue, Dallas, Texas. All shareholders are cordially invited to attend.

FORM 10-K:

Shareholders may obtain a copy, exclusive of exhibits, of the Form 10-K Annual Report for the year ended December 31, 1979, filed with the Securities and Exchange Commission, by writing to the Financial Relations Department at the Company's mailing address.

AUTOMATIC STOCK PURCHASE PLAN:

This plan provides a simple, convenient, and inexpensive way for shareholders to invest cash dividends and additional cash deposits in Southland shares. For further information, write the Financial Relations Department at the Company's mailing address.

MAILING ADDRESS:

P.O. Box 719, Dallas, Texas 75221

TELEPHONE:

(214) 828-7011





THE SOUTHLAND CORPORATION 1979 ANNUAL REPORT
2828 NORTH HASKELL • DALLAS, TEXAS 75204